

Czech regulation of limited companies from the point of view of the 'law and economics' school

Abstract

Law and economics has a potential to provide us with an uncommon and to the Czech jurisdiction often neglected point of view on laws. The aim of this paper is to apply economic theories on directors' liability for breach of fiduciary duties and to consider its consequences on the economic efficiency of companies. The critical question is whether not having such liability could provoke an increase of wealth of all stakeholders. The paper also aims to come up with instruments capable of minimizing the lost caused to companies by mandatory rules regarding director's liability. At the end of the thesis, the Czech laws regarding the director's liability for breach of fiduciary duties are analyzed in the point of view of economic analysis. The analysis is followed by proposition of instruments that could make companies operating in Czech legal environment more effective.

Directors' liability, which can result in an aversion to make risky decisions, can cause significant losses to companies (so called agency costs). For that reason, the possibility to determine the scope of director's liability given to shareholders can have, in some cases, positive effect on the company's efficiency. The paper concludes that the possibility to exclude director's liability for breach of duty of loyalty can hardly be effective for the society. However, it is not an easy task to give a clear conclusion about the possibility to exclude the duty of care. It appears that non-legal instruments capable to reduce agency costs could be effective in this case. Nevertheless, the risk of negative outcomes for other stakeholders is also present.

Even in case of keeping the mandatory liability rules there are instruments that could considerably reduce the costs incurred by them. One of them is the possibility to insure directors against the liability for breach of fiduciary duties, or better said the duty of care. Moreover, significant power in this matter is given to judges who can by lenient decisions also substantially decrease the losses caused by mandatory liability rules.

Key words: law and economics, fiduciary duties, agency costs, directors' liability